(17)

No. 91-615

In The

Supreme Court of the United States

October Term, 1991

ALLIED-SIGNAL, INC.,
as successor-in-interest to
The Bendix Corporation,

Petitioner,

v.

DIRECTOR, DIVISION OF TAXATION,

Respondent.

On Writ Of Certiorari To The Supreme Court Of New Jersey

REPLY BRIEF FOR RESPONDENT ON REARGUMENT

Robert J. Del Tufo
Attorney General of New Jersey
Attorney for Respondent
Division of Law
R.J. Hughes Justice Complex
CN 112
Trenton, New Jersey 08625
(609) 292-1527

Joseph L. Yannotti
Assistant Attorney General
Of Counsel

Mary R. Hamill*
Sarah T. Darrow
Margaret A. Holland
Deputy Attorneys General
On the Brief

*Counsel of Record

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ARGUMENT

POINT I

IN REQUIRING AN OPERATING RELATIONSHIP BETWEEN THE PAYOR AND PAYEE OF INTANGIBLES INCOME, *ASARCO* AND *WOOLWORTH* ARE INCONSISTENT WITH THE CONSTITUTIONAL CONSTRAINTS TRADITIONALLY IMPOSED ON THE STATES' TAXING POWER AND WITH EXISTING STATE TAX SCHEMES.

A. *ASARCO* and *Woolworth* Do Not Follow Logically from the Court's Cases Interpreting the Due Process Clause.

Petitioner's discomfort with the holdings of *ASARCO Inc. v. Idaho State Tax Comm'n*, 485 *U.S.* 307 (1982) and *F.W. Woolworth Co. v. Taxation & Revenue Dep't*, 458 *U.S.* 354 (1982) is evident. It now maintains that the "essential holding" of the two cases is a rejection of the states' argument that the corporate purpose of an investment should determine its unitary character (Psb6)[1] and concedes that operating relationships between the payor and payee of investment income are not always necessary (Psb5 n.1).[2] Essentially, petitioner has abandoned its defense of the *ASARCO/Woolworth* payor-payee rule (*cf.* Pb15,23) and offers no response to New Jersey's argument that the payor-payee rule is not required by the Due Process Clause, is inconsistent with the Court's

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[1] The designation "Psb" refers to petitioner's supplemental brief on reargument.

[2] Petitioner, in fact, no longer disagrees with the proposition that the integration of an intangible with the taxpayer's unitary operations establishes that income from the intangible is apportionable (Psb11,18).

prior and subsequent decisions involving the unitary business principle, and has caused extensive litigation in the lower courts (Rsb12-14). This litigation results from the fact that the payor-payee rule cannot be squared with the definition in the Uniform Division of Income for Tax Purposes Act (UDITPA) of apportionable business income (*see* Rb 34) nor with the full apportionment states' statutory schemes permitting the inclusion of all income in the preapportionment tax base.[3] Moreover, the rule defies the common sense and experience of lower court judges and state tax administrators.

Petitioner asserts that *ASARCO* and *Woolworth's* rejection of the corporate purpose definition of a unitary investment derives from the fundamental requirement of the Due Process Clause that a state cannot tax activities lacking a minimum connection with the taxing state (Psb6). While that may be the rule of the Due Process Clause for state tax purposes, the Court's seminal cases construing the Clause do not hold that, once a taxpayer is doing business within a nondomiciliary taxing state, there must be a separate nexus with each and every out-of-state activity of the taxpayer in order for the state to include the income generated in part by that activity in the preapportionment tax base. *Miller Bros. Co. v. Maryland,* 347 *U.S.* 340, 344-45 (1954); *Wisconsin v. J.C. Penney Co.,* 311 *U.S.* 435, 444-45 (1940); *Northwestern States Portland Cement Co. v. Minnesota,* 358 *U.S.* 450, 460, 464-65

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[3] Petitioner (Psb5-6) and some of the *amici curiae* assume that the overruling of *ASARCO* and *Woolworth* would entail a complete jettisoning of the unitary business principle, but that is not necessarily the case. One alternative would be to abandon the payor-payee rule but retain the remaining elements of the unitary business principle, facing up to the fact that difficult, sometimes arbitrary, lines would have to be drawn.

(1959). The protections and benefits extended by a nondomiciliary state to the taxpayer justify imposition of an apportioned tax on the taxpayer's income. *Id.*

B. Property Tax Principles Cannot be Transplanted Wholesale To Cases Involving Net Income Taxes.

With the exception of *ASARCO* and *Woolworth,* the Court's unitary business cases involving corporate net income taxes have not required an "organic connection" between a nondomiciliary taxpayer's in-state and out-of-state activities (Rsb 30-33). The Court has found a sufficient connection by reason of the nature of a taxpayer's business, *see e.g. Mobil Oil Corp. v. Comm'r of Taxes,* 445 *U.S.* 425, 435 (1980), or the operational nature of an investment. *Container Corp. v. Franchise Tax Bd.,* 463 *U.S.* 159, 180 n.19 (1983). Mere "unity of ownership and management" may suffice. *Butler Bros. v. McColgan,* 315 *U.S.* 501, 508 (1942), and so may "largely unquantifiable transfers of value." *Container,* 463 *U.S.* at 164-65.

Petitioner's reliance on the early railroad property tax cases is misplaced because tangible property taxes involve the valuation of specific property located at a specific place on a specific day, while the attribution of net income involves an attempt to locate something that has no physical properties in and of itself, whose "location" can be determined only indirectly. *Wheeling Steel Corp. v. Fox,* 298 *U.S.* 193, 212 (1936). Thus, where the value of a corporation's stock was used to determine the value of its property within the taxing state, property such as bonds held outside the state and having no "organic connection" to the in-state property could not be

included in the total value which was to be apportioned by means of a mileage formula. *Fargo v. Hart,* 193 *U.S.* 490, 499, 501 (1904). Inclusion of the bonds in the tax base produced an apportioned value of more than $800,000, while the actual value of the corporation's tangible property within the taxing state amounted to less than $8,000. *Id.* at 497. On the other hand, where the state sought to impose a franchise tax measured by the value of a corporation's capital stock, the Court held that all the corporation's assets could be included despite the fact that the statutory formula allocated $23 million to the taxing state and the actual value of the corporation's in-state assets was approximately $3 million. *Ford Motor Co. v. Beauchamp,* 308 *U.S.* 331, 334 (1939).

Determining the source of a corporation's in-state net income is as elusive as determining the value of a state franchise. On a separate accounting basis, there may even be a loss within the taxing state, and yet, under the unitary business principle, income may be attributed to the state. *Butler Bros.,* 315 *U.S.* at 506-07. In short, the Court has consistently rejected in the net income tax context the kind of direct, operating link that petitioner seems to believe must be present in order to apportion income from intangibles. Petitioner's "organic connection" rule would reject the reasoning of the Court's unitary business cases involving net income taxes.

C. Corporate Purpose, As Defined in *Container,* Would Be An Appropriate Test In The Single Entity Context But For The Impossibility of Drawing a Clear Line.

Although petitioner maintains that *ASARCO* and *Woolworth* properly rejected a unitary business principle

founded on the purpose for which an investment is made, at the same time petitioner seems to adopt the corporate purpose doctrine described in *Container* (Psb18). In discussing Container's loans to its subsidiaries, the Court stated that the loans were made "to ensure that '[t]he overseas operations of [appellant] continued to grow and to become a more substantial part of the company's strength and profitability.' " *Container*, 463 *U.S.* at 180 n.19. Citing *Corn Products Refining Co. v. Comm'r*, 350 *U.S.* 46, 50-53 (1955), the Court suggested that "capital transactions can serve either an investment function or an operational function." *Id.* Thus, a business function or motive, which seems no different than a business purpose, can convert what would otherwise be a passive to an operational investment. Properly applied, this is the test we advocated in our initial brief (Rb18-19, 41-43), and we pointed out that Bendix' purchase of stock in ASARCO served three operational functions - further diversification of the company, generation of capital for one of Bendix' core businesses, and as a means of acquiring knowledge of ASARCO and the nonferrous metals business before enlarging or disposing of the investment. These purposes were no different, we pointed out, than Container's loans to its subsidiaries, which were made for the purpose of making the subsidiaries a more substantial part of the corporation (Rb42).

The difficulty of drawing a clear, predictable line between a capital transaction serving "an investment function" and one serving "an operational function," *Container*, 436 *U.S.* at 180 n.19, precisely the same difficulty that the Court confronted and resolved in *Arkansas Best Corp. v. Comm'r*, 485 *U.S.* 212 (1988), involving the *Corn Products* exception to the statutory definition of

capital asset (Rsb45), leads us to believe that a more workable, fair, and economically real place to draw the line is at the corporate entity.

POINT II

NEW JERSEY'S PROPOSED RULE OF FULL APPORTIONMENT WITHIN SINGLE CORPORATE ENTITIES WOULD NOT DISRUPT OR RENDER UNCONSTITUTIONAL EXISTING STATE TAX SCHEMES.

Petitioner suggests that the existing scheme for taxing multistate corporations is well settled and uniform (Psb14-21) and that any change would render the majority of the states' current tax schemes unconstitutional (Psb27) and would create intractable apportionment problems (Psb25, 31).

A brief reiteration of the rule we propose makes clear that many of petitioner's fears would not materialize. As to single corporate entities, the rule would permit a nondomiciliary state to include in the preapportionment tax base all the income of a multistate corporation doing business within that state. As all the income, not just income from intangibles, would be apportionable, none of the "form versus substance" problems suggested by petitioner (Psb23-24) would arise. The rule would simply permit a state to extend its taxing power to all the income of a nondomiciliary taxpayer doing business within it. The fact that the UDITPA states, by statute, allocate 100% of nonbusiness income to the commercial domicile would not render those statutes facially unconstitutional because the Court has held that the mere possibility of double taxation in a net income context is constitutionally acceptable. *Moorman Mfg. Co. v. Bair*, 437 *U.S.* 267, 276-80

(1978). Thus, the constitutional havoc envisioned by petitioner (Psb27-30) would not materialize, nor would the "devastating liability for refunds" if the overruling of *ASARCO* and *Woolworth* were given retroactive effect (Psb47). We recognize that our proposed rule may increase the risk of multiple taxation of intangibles income and might require greater attention to the apportionment formula, but both of those problems exist currently, and should be dealt with in individual cases if and when they arise.

A. The Present Scheme of Taxing Intangibles Income Is Not Uniform.

Petitioner exaggerates in claiming that "the vast majority of states explicitly recognize the distinction between apportionable and allocable investment income . . . " (Psb16). In fact, 16 states, including New Jersey, apportion all or nearly all income from intangibles.[4] This would seem to be a rather substantial minority, whose taxing schemes are entitled to as much respect as the schemes of the majority that distinguish between business and nonbusiness income. *See Moorman* (sustaining Iowa's single-factor apportionment formula).[5]

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[4] The full apportionment states other than New Jersey include Connecticut, Maine, Maryland, Massachusetts, Michigan, New Hampshire, New York, Ohio, Rhode Island, Texas, and Vermont. Minnesota, Nebraska, Virginia, and Wisconsin apportion nearly all income. *See* the appendix to this brief at Rrsa 6a-8a and 1 *Multistate Corporate Income Tax Guide* ¶167 (CCH).

[5] Only Nebraska and Texas, in addition to Iowa, use a single-factor apportionment formula. 1 *Multistate Corporate Income Tax Guide* ¶146 (CCH).

Petitioner's statement that the "prevailing pattern" ensures that there will be neither undertaxation nor overtaxation of investment income (Psb17) is not consistent with the impressions of state tax administrators that the present system results in substantial undertaxation of intangibles income. *See* the initial Brief *Amicus Curiae* of Multistate Tax Commission in Support of Respondent at 23 n.8; *ASARCO,* 458 *U.S.* at 345 (O'Connor, J., dissenting); Dexter, "Taxation of Income from Intangibles of Multistate-Multinational Corporations," 29 *Vand. L. Rev.* 401, 403 (1976). This is a case in point since Michigan apportioned Bendix' gain on the ASARCO stock sale, and under the *ASARCO/Woolworth* payor-payee rule, no other state would tax the income.[6]

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[6] Included in the appendix to this brief is a chart showing the state of commercial domicile of each of the corporations that have joined in an *amicus* brief at this stage of the proceedings (Rrsa 9a-10a). Of the 32 corporations, 20 have their corporate domiciles in states that apportion, or largely apportion, investment incomes; 10 of the remaining 12 are headquartered in states that, while allocating investment income to the commercial domicile, exclude or largely exclude dividend income, and of the remaining two, Chevron Corporation, headquartered in California, has filed an *amicus* brief in support of New Jersey urging presumptive full apportionment of intangibles income. *See* Rrsa 1a-8a showing the full apportionment states, the UDITPA states, and the exclusions for dividend income. One has to wonder about multistate corporations' claims of excessive state taxation of investment income (Pb42; Psb30) unless there is a constitutional right, of which we are unaware, to pay tax on less than 100% of investment income. *Cf.* Brief of *Amici Curiae* in support of Petitioner by American Home Products Corporation *et al.* at 2, expressing the concern that "all of [*amici's*] intangible income would be apportionable by nondomiciliary States."

Under the internal consistency test, an apportionment formula, if applied by all the states, cannot result in more than 100% of a corporation's income being subjected to tax. *Container*, 463 *U.S.* at 169. The "prevailing pattern," particularly if the *ASARCO/Woolworth* payor-payee rule is strictly applied, results in far less than 100% of a corporation's income being subjected to tax because large amounts of intangibles income are removed from the base before the apportionment formula is applied. The "prevailing pattern" is not workable (Rsb12), is certainly not equitable to the states, is not "substantially uniform," and above all, has no relation to economic reality (Rsb11,42), a point that petitioner does not address.

B. The State of Commercial Domicile Has No Paramount Right To Tax Intangibles Income.

Petitioner's argument that the commercial domicile somehow offers benefits and protections justifying taxation of 100% of so-called nonbusiness income was rejected in *Mobil*, 445 *U.S.* at 445-46. New Jersey offered substantial protections and benefits to Bendix' aerospace and industrial energy divisions, protections and benefits which made it possible for Bendix to earn 8% of its net income in the State. The protections and benefits extended by New Jersey entitle it to "ask return" commensurate with the business conducted there, *J.C. Penney Co.*, 311 *U.S.* at 444-45, and the ASARCO investment was part of that business.[7]

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[7] It is not true that Bendix managed its investments exclusively at its commercial domicile in Michigan (cf.

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At bottom, petitioner's theory that the state of commercial domicile has a paramount right to tax income from intangibles rests on the misconception that corporate investing is somehow segregated from corporate operations. As we made clear in our initial brief, the record in this case belies the notion because it establishes that Bendix had a corporate function of investing in other corporations as a means of diversification and growth. The Bendix CEO viewed the corporation as consisting of pools of assets, including both operating assets and investment assets (J.A. 137). As we indicated in our supplemental brief, Bendix' mixing of investment and operational strategies is not unique. The line between operations and investments is fuzzy from an accounting standpoint, and corporate investing is on a continuum (Rsb42-43). Petitioner may be right that 55 years ago, in the context of property tax valuation methods, there was such a thing as "assets of an interstate corporation [that] are . . . completely divorced from the interstate business . . . ," but that does not appear to be true today. *Cf.* 2 J. Bonbright, *Valuation of Property*, 660 (1937) (quoted at Psb13),[8] but *see* Dexter, *supra* at 413, 418. As petitioner

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Psb20 n.10). The Lehman Brothers account into which the proceeds of Bendix' various stock sales were placed was presumably managed in New York City where Lehman Brothers was located (J.A. 181 ¶117).

[8] Professor Bonbright goes on to recognize that there is no sharp line between assets that contribute to the whole system and those that do not, Bonbright, *supra* at 661, and concludes that, since the question is one of degree and gradations that "are not sharply defined, practical expediency requires frankly arbitrary rules rather than theoretically satisfying solutions." *Id.*

itself has recognized, the 1980's witnessed "a significant increase in the scope and size of corporate diversification" (Pb41-42).

C. Freeing the States To Apportion All Income of Nondomiciliary Corporations Would Not Render the UDITPA States' Tax Schemes Unconstitutional.

Petitioner suggests (Psb27) that a rule permitting the states to apportion all intangibles income would render unconstitutional the laws of a majority of the states that distinguish between business and nonbusiness income because the income would be doubly taxed, once in full at the corporate domicile and again on an apportioned basis in a full apportionment state. But in the context of a corporate net income tax, the risk of double taxation, *Moorman*, 437 *U.S.* at 278-79, or even actual double taxation, *Container*, 463 *U.S.* at 187-88 and n.22, does not necessarily render either state's tax unconstitutional. Although, "[t]axation by apportionment and taxation by allocation to a single situs are theoretically incommensurate," *Mobil*, 445 *U.S.* at 444, the rule to date appears to apply only to *movable* tangible property such as boats and barges, *Standard Oil Co. v. Peck*, 342 *U.S.* 382 (1952), and freight cars. *Central Railroad Co. of Pennsylvania v. Pennsylvania*, 370 *U.S.* 607 (1962). In the context of a net income tax, *Moorman* and *Container* suggest that theoretical claims of double taxation, with no factual showing of an "existing duplicative tax," *Mobil*, 445 *U.S.* at 444, cannot succeed.

As made clear in the appendix to our supplemental brief (Rsa21a-23a), allegations of double taxation of intangibles income to date have been relatively infrequent even though the potential for double taxation inheres in

the present system. *Moorman,* 437 *U.S.* at 279. As indicated in the appendix to this brief (Rrsa1a-5a), of the 28 states that allocate 100% of nonbusiness income to the commercial domicile, 16 exclude 70% or more of dividend income from the tax base, thereby substantially reducing the risk of double taxation, and 11 of the 16 states that apportion all or nearly all intangibles income exclude at least 50% of dividend income from the tax base, thereby further reducing the risk of double taxation. See *supra* n. 6. Moreover, a UDITPA state, faced with a claim of double taxation by a domiciliary taxpayer, might well offer a credit or some other adjustment under UDITPA's discretionary relief provision. 7A *Uniform Laws Annotated* 355 (West 1985), *UDIPTA* § 18. Thus, double taxation is not the inevitable result of full apportionment. *Container,* 463 *U.S.* at 188, 192-93.

In sum, the Constitution, through the Due Process and Commerce Clauses, merely limits a state's taxing power. P. Hartman, *Federal Limitations on State and Local Taxation,* 12, 14, 17-19, 21 (1981); Hellerstein, "State Taxation of Interstate Business: Perspectives on Two Centuries of Constitutional Adjudication," 41 *Tax Lawyer* 37, 40, 50, 74 (1987). The Constitution does not *require* the states to extend their taxing power, does not mandate a single, uniform apportionment rule, *Moorman,* 437 *U.S.* at 279, and does not, in the context of a state corporate net income tax, condemn a taxing scheme that may produce, or even does produce, instances of double taxation. *Container,* 463 *U.S.* at 187-93.[9] Whether our proposed rule

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[9] Petitioner's notion that a rule permitting some states to fully apportion intangibles income while others taxed it in full

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would result in actual double taxation should abide a record demonstrating that fact. Here, due to the fact that Michigan apportioned the ASARCO gain, there is no evidence whatever of double taxation.

D. Full Apportionment Would Not Necessarily Be Unfair.

Petitioner asserts that the apportionment of all intangibles income would violate the external consistency test (Psb25) and, if extended to the apportionment of both operating and intangibles income, would lead to gross misattributions of income (Psb31-33). Petitioner's argument on both scores is grounded in its belief that intangibles income and operating income earned within a single corporate entity may indeed be unrelated to the unitary business being conducted in the taxing state.[10] The record in this case, modern business' approach to corporate investing (Rsb42-43),[11] the inability of the accounting profession to pigeonhole investing and operating activities (Rsb43-44), and the potential for manipulation inherent in

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at the commercial domicile would produce a tax of 200% on investment income would materialize only if the state of the corporation's domicile were the only remaining state to distinguish between business and nonbusiness income, while every other state had adopted full apportionment. Moreover, the figure assumes that no state would exclude the intangibles income and that the state of commercial domicile would refuse any relief in the face of clear evidence of multiple taxation.

[10] Petitioner's appendix reflects the same conceptual flaw: Depending upon the facts, a UDITPA state may treat intangibles income as apportionable business income.

[11] The designation "Rsb" refers to respondent's supplemental brief on reargument.

a constitutional rule under which large amounts of income are in or out of the tax base depending upon considerations of business motive (Rsb44-45) strongly suggest that there are no economically real distinctions between various corporate activities and that, if distinctions are to be made, they are essentially arbitrary. Bonbright, *supra*, at 661. Scholarly commentary agrees. Frank Keesling, one of the "distinguished students" cited by petitioner as authority for the proposition that investment income should not be included in the apportionable tax base (Psb13), subsequently came to the opposite conclusion, suggesting that it might be preferable to apportion income from securities purchased to promote a corporation's business. Keesling, "The Impact of the *Mobil* Case on Apportionment of Income," 1981 *B.Y.U.L. Rev.* 87, 99. In an earlier article, Mr. Keesling questioned "whether there is such a thing as a non-unitary business," stating:

> Wherever there is common ownership there is a certain amount of common management, centralized performance of certain functions, and other indications of integration. [Keesling, "A Current Look At The Combined Report and Uniformity in Allocation Practices," 42 *J. of Taxation* 106, 109 (Feb. 1975)].

To the extent that intangibles constitute part of a unitary business, the standard three-factor apportionment formula may be viewed as properly assigning the income of a multistate corporate taxpayer among the jurisdictions where it does business. J. Hellerstein, *State Taxation I Corporate Income and Franchise Taxes*, 559 (1983). If the unitary business is deemed to be congruent with the corporate entity, the three-factor formula, without

adjustment, may continue to provide a fair apportionment (Rsb37). *See* Dexter, *supra* at 407, 411-12, 418, 420.

On the other hand, if inclusion of intangibles income in the preapportionment tax base and application of the standard three-factor formula does in fact attribute too much intangibles income to a particular state, state courts are quite able to deal with the problem. For example, in *F.W. Woolworth Co. v. Director, Div. of Taxation*, 45 *N.J.* 466, 499, 213 *A.*2d 1, 19 (1965), the New Jersey Supreme Court remanded the case for consideration of factor relief after concluding that the dividends from Woolworth's foreign subsidiaries were unitary income.[12] Since the lower

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[12] Subsequent to New Jersey's *Woolworth* case, the New Jersey Legislature enacted the 100% dividend exclusion for dividends from subsidiaries owned to the extent of 80% or more. 1968 *Laws of New Jersey*, ch. 250; *N.J. Stat. Ann.* 54:10A-4(k)(5) (West 1986).

Other cases in which state courts have provided for factor relief after including intangibles income in the preapportionment tax base include *People ex rel. Alpha Portland Cement Co. v. Knapp*, 230 *N.Y.* 48, 129 *N.E.* 202 (1920) (invalidating statutory provisions that included investment income without including investment values in formula); *American Tel. & Tel. Co. v. Wisconsin Dep't of Revenue*, 143 *Wis.*2d 553, 422 *N.W.*2d 629, 636-37 (Wis. App. 1988) (invalidating apportionment formula under external consistency test where public utility had $500 million in operating income and nearly $3 billion in dividend income from subsidiaries, and remanding to revenue department to determine a fair apportionment); *NCR Corp. v. Comptroller of the Treasury*, 313 *Md.* 118, 154, 544 *A.*2d 764, 781 (1988) (remanding to state tax court to adjust apportionment formula where dividends from foreign subsidiaries were included in preapportionment tax base); *NCR Corp. v. South Carolina Tax Comm'n*, 304 S.C. 1, 402 *S.E.*2d 666, 673-74 (1991) (remanding to lower court to adjust apportionment formula where income from

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courts are fully capable of dealing with fair apportionment issues, there is no need for the Court to prohibit full apportionment of income within a single corporate entity on the ground that the external consistency test would be routinely violated.

Nor can it be convincingly maintained that full apportionment of all income earned by separate corporations results in gross misattributions of income (Psb 31-33). Again, the justification for full apportionment is the impossibility of segregating distinct corporate activities that are linked by common ownership and common management. Where these factors exist, i.e. within a single corporation, apportioning the income among the states continues to "bear[] some resemblance . . . to slicing a shadow." *Container*, 463 *U.S.* at 192. Thus, the "practical [and] theoretical justification" for apportionment, *Trinova Corp. v. Michigan Dep't of Treasury*, 111 *S.Ct.* 818, 829 (1991), continues to exist and in fact militates in favor of full apportionment of all income within a single corporation (*cf.* Psb32).

POINT III

STARE DECISIS DOES NOT REQUIRE ADHERENCE TO *ASARCO* AND *WOOLWORTH* BECAUSE NEITHER SUBSTANTIVE PROPERTY LAW NOR CONTRACT RIGHTS ARE INVOLVED.

As we demonstrated in our initial brief, considerations of *stare decisis* should not impede the overruling of

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foreign subsidiaries was included in preapportionment tax base); *Tambrands Inc. v. State Tax Assessor*, 595 *A.*2d 1039, 1045 (Me. 1991)(remanding to taxing authority to "include additional factors in the apportionment formula" because dividends from foreign affiliates that were taxed by foreign countries were included in the preapportionment tax base).

ASARCO and *Woolworth* because the cases were badly reasoned, have proved to be inconsistent with economic reality, and have produced incoherent, inconsistent results in the lower courts.

Petitioner maintains that the two cases should stand because the rules at issue "involve property interests" where it is necessary for people to be able to predict the legal consequences of their actions (Psb36). But *ASARCO* and *Woolworth* do not involve simply property interests, and they certainly do not involve "substantive property law as such . . . " *Oregon ex rel. State Land Bd. v. Corvallis Sand & Gravel Co.*, 429 *U.S.* 363, 381 (1977). Rather, the issue relates to business taxpayers' expectations in the face of the states' taxing power. "In cases such as this, considerations of *stare decisis* play a less important role than they do in cases involving substantive property law." *Id.*

Moreover, to the extent that *ASARCO* and *Woolworth* are out of sync with the Court's preceding and subsequent unitary business cases, a return to the proper rule should conform more closely to business taxpayers' reasonable expectations. *Id.* at 382. Taxpayers plainly have no contract or property rights in a specific level of taxation. *Welch v. Henry*, 305 *U.S.* 134, 146 (1938). If it were otherwise, Congress could not enact tax statutes that apply to periods prior to enactment, which it has done repeatedly. *United States v. Darusmont*, 449 *U.S.* 292, 296, (1981). Nor can petitioner reasonably claim that it or any other business taxpayer legitimately relied on the *ASARCO/Woolworth* payor-payee rule when the rulings

provoked repeated litigation in the lower courts (Rsa21a-25a).[13]

POINT IV

***ASARCO* AND *WOOLWORTH* SHOULD BE OVERRULED RETROACTIVELY BECAUSE LITIGANTS DID NOT LEGITIMATELY RELY ON THE TWO DECISIONS.**

In arguing that *ASARCO* and *Woolworth* should be overruled prospectively under *Chevron Oil Co. v. Huson,* 404 *U.S.* 97 (1971), petitioner virtually assumes that an overruling decision would "establish a new principle of law . . . by overruling clear past precedent on which litigants may have relied. . . . " *Id.* at 106-07. But as we pointed out in our supplemental brief, Bendix could not possibly have relied on *ASARCO* and *Woolworth* when it decided to sell the ASARCO stock because the decision to sell was made before *ASARCO* and *Woolworth* were handed down (Rsb18). Nor is it accurate to say that *Container* did not cast doubt on the continuing vitality of the two decisions. *See id.* at n. 7. The Court's brief reference to *ASARCO* in *Trinova,* 111 *S.Ct.* 834, for the proposition that Michigan's single business tax did not tax " 'value earned outside [Michigan's] borders' " hardly amounts to a reaffirmation of the *ASARCO/Woolworth* payor-payee rule.

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[13] Petitioner now advises that virtually all the lower courts followed *ASARCO* and *Woolworth* (Psb38), but in its petition for *certiorari* petitioner pointed to the conflicting decisions in the lower courts (Pet. at 13) and claimed that "many state court decisions . . . reflect both uncertainty and confusion regarding the [applicable] constitutional constraints . . . ." (Pet. at 16).

As to whether retroactive application will further a rule extending the states' taxing power, at least to the extent that states have assessed and denied refunds in the belief that *ASARCO* and *Woolworth* did not preclude them from taxing an apportioned share of intangibles income, retroactive application would seem to further the new rule. Otherwise, as we stated previously, while prevailing on the legal principle, the states could be exposed to substantial refund claims and could lose the assessment cases currently pending (Rsb19-20).

Contrary to petitioner's claim (Psb47), the equities do not favor prospective overruling. Nine of the 16 full apportionment states exclude between 70% and 100% of dividend income and two others (New York and New Jersey) exclude between 50% and 100% of dividend income (Rrsa6a-8a). Thus, as to the major category of recurring intangibles income, most of the full apportionment states would not be making retroactive assesssments if *ASARCO* and *Woolworth* were overruled retroactively. Moreover, as made clear in the appendix to our supplemental brief (Rsa21a-25a), the includability of capital gains and interest income has been actively litigated in the full apportionment states. *See* also Brief for *Amici Curiae* Massachusetts *et al.* Supporting Respondent at 4. Thus, multistate taxpayers in those states cannot claim surprise that their intangibles income would continue to be assessed by those states. As to refunds owing to domiciliary taxpayers in states that allocate 100% of nonbusiness income to the commercial domicile, more than half of these states already exclude between 70% and 100% of dividend income (Rrsa1a-5a). Further, as we have said previously, our proposed rule would not render the UDITPA states' statutes automatically unconstitutional

and thus these allocating states would not be exposed to massive refund claims.

CONCLUSION

For the foregoing reasons, the judgment of the Supreme Court of New Jersey should be affirmed, *ASARCO* and *Woolworth* should be overruled retroactively, and the states should be permitted to apportion all the income of nondomiciliary corporations doing business within their borders.

Respectfully submitted,

ROBERT J. DEL TUFO
Attorney General of New Jersey
Attorney for Respondent

MARY R. HAMILL
Counsel of Record
SARAH T. DARROW
MARGARET A. HOLLAND
Deputy Attorneys General
On the Brief

Division of Law
Hughes Justice Complex
CN 112
Trenton, New Jersey 08625
(609) 292-1527

JOSEPH L. YANNOTTI
Assistant Attorney General
Of Counsel

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Dividend Income Deducted or Excluded from Corporate Income Taxation in States That Distinguish Between Business and Non-Business Income*

State	Special fed. deduction adopted?**	Any State Dividend Exclusion?
AL	No	Exclusion for dividends from 50% subsidiaries. Ala. Code § 40-18-35(a)(14).
AK	Yes, 70-100% excluded.	No
AZ	No	Exclusion for dividends from Az. taxed payor; from controlled payor if commercial domicile in Az. or, if commercial domicile outside Az. 50% in 1990 and 100% thereafter. Ariz. Rev. Stat. Ann. § 43-1122 and § 43-1128.

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* Sources: *Multistate Corporate Income Tax Guide* ¶ 79 (CCH); state statutes cited herein.

** Pursuant to IRC § 243, a corporation may deduct from its taxable income 100% of qualifying dividends received from a member of its affiliated group, 100% of dividends received by a small business investing company, and 70% of all other dividends. The Code also provides for deductions of dividends received on certain preferred stock, IRC § 244, and from certain foreign corporations, IRC § 245. Where a "Yes" is included in this column, the State has adopted these federal deductions and, thus, excludes 70-100% of all dividends from taxable income.

State	Special fed. deduction adopted?	Any State Dividend Exclusion?
AR	No	Exclusion for dividends from 95% subsid. and on stock of capital development corporations. Ark. Code Ann. § 26-51-404(b)(9) and § 15-4-1025.
CA	No	Amount of exclusion depends on degree of affiliation with payor B for dividends from Cal.-taxed payor; exclusion for intercompany dividends in combined report, and for dividends from certain foreign construction projects. Cal. Rev. and Tax. Code § 24402, § 24411 and § 25106.
CO	Yes, 70-100% excluded.	No
FL	Yes, 70-100% excluded.	No
HI	No	Partial or total exclusion for dividends from controlled payor. Haw. Rev. Stat. § 235-7(c).

State	Special fed. deduction adopted?	Any State Dividend Exclusion?
ID	No	Partial exclusion for dividends from Idaho-taxed payor; special provisions under water's edge election. Idaho Code § 63-3022(e) and (f).
IL	Yes, 70-100% excluded.	Plus foreign dividends excluded. Ill. Income Tax Act § 203(b)(2).
IN	Yes, 70-100% excluded.	Plus partial or total exclusion of foreign dividends. Ind. Code Ann. § 6-3-2-12.
IA	Yes, 70-100% excluded.	No
KS	Yes, 70-100% excluded.	Plus 80% exclusion of post-1987 foreign dividends. Kan. Stat. Ann. § 79-32,138.
KY	No	All dividends excluded. Ky. Rev. Stat. Ann. § 141.010(12)(b).
MS	No	All dividends taxed except from issuers taxed by Mississippi and certain dividends from investment trusts. Miss. Code Ann. § 27-7-15(1) and (4).

State	Special fed. deduction adopted?	Any State Dividend Exclusion?
MO	Yes, 70-100% excluded.	Plus exclusion of all corporate dividends from sources w/in Missouri. Mo. Ann. Stat. § 143.431.
MT	Yes,* 70-100% excluded.	Plus 80% exclusion of all apportionable dividends and water's edge election. Mont. Code Ann. § 15-31-325.
NM	Yes, 70-100% excluded.	No
NC	No	Exclusion dependent upon percentage of business done in N.C. by payor. N.C. Gen. Stat. § 105-130.7; See, *Multistate Corporate Income Tax Guide,* ¶ 3708.21 (CCH).
ND	No	Exclusion for dividends from N.D. N.D. Cent. Code § 57-38-01.3(1)(g).
OK	Yes, 70-100% excluded.	No
OR	No	Exclusion for 70% of all dividends except for certain specific types; 80% deductible if from 20% owned payor. Or. Rev. Stat. § 317.267.

* In *Baker Bancorporation, Inc. v. Dept. of Rev.*, 657 P.2d 89 (1982), the Montana Supreme Court ruled that the federal dividend deductions are allowed, since they are not expressly disallowed by Montana's tax law.

State	Special fed. deduction adopted?	Any State Dividend Exclusion?
PA	No	Exclusion for all dividends. Pa. Stat. Ann. Tit. 72, § 7401(3)1(a) and (b).
SC	Yes, 70-100% excluded.	But, foreign dividend gross-up not deductible. S.C. Code Ann. § 12-7-430.
SD	No	Exclusion for dividends received from financial institutions subject to S.D. franchise tax. S.D. Codified Laws Ann. § 10-43-10.2(7) and § 10-43-10.3(2).
TN	No	Exclusion for dividends from 80% owned subsidiary only. Tenn. Code Ann. § 67-4-805(b)(2)(A).
UT	No	100% exclusion of dividends from non-unitary subsidiaries plus water's edge election. Utah Code Ann. § 59-7-106(2)(d).
WV	Yes, 70-100% excluded.	No

Dividend Income Deducted or Excluded from Corporate Income Taxation in States That Apportion All or Nearly All Income*

STATE	DIVIDEND DEDUCTION OR EXCLUSION
CT	100% exclusion of all dividends, except that no exclusion is allowed for 30% of dividends from domestic corporation in which taxpayer owns less than 20%. Conn. Gen. Stat. Ann. § 12-217.
ME	Federal dividend deduction** plus phased in subtraction ('89-'93) for apportionable dividends from affiliates not included in combined report. Me. Rev. Stat. Ann. tit. 36 § 5200-A.2(G).
MD	Federal dividend deduction plus subtraction for dividends from controlled foreign corp. and from DISCs. Md. Code Ann., Tax-Gen. § 10-307.
MA	Dividends 95% deductible except for dividends from (1) less than 15% owned corp., (2) Mass. Corp. trust, and (3) non-wholly owned DISCs. Mass. Gen. Laws Ann. ch. 63, § 38(a).
MI	Exclusion for all dividends. Mich. Comp. Laws Ann. § 208.9(7)(a).

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* Sources: *Multistate Corporate Income Tax Guide* ¶ 79 (CCH); state statutes cited herein.

** Pursuant to IRC § 243, a corporation may deduct from its taxable income 100% of qualifying dividends received from a member of its affiliated group, 100% of dividends received by a small business investing company, and 70% of all other dividends. The Code also provides for deductions of dividends received on certain preferred stock, IRC § 244, and from certain foreign corporations, IRC § 245. The States which have adopted these federal deductions thus exclude 70-100% of all dividends from taxable income.

STATE	DIVIDEND DEDUCTION OR EXCLUSION
MN	80% deductible if from 20% owned payor and stock from which paid meets certain conditions; 70% deductible if from less than 20% owned payor; remaining "excess qualifying dividends" if from insurance or investment company that is member of same affiliated group and dividends are eliminated in federal consolidation. Minn. Stat. Ann. § 290.21.4.
NE	Federal dividend deduction plus exclusions of dividends from foreign corporations. Neb. Rev. Stat. § 77-2734.04(6) and § 77-2734.08.
NH	Exclusion for (1) dividends received by parent if subsidiary subject to tax or not unitary, (2) deemed DISC subject to tax, and (3) dividends from foreign affiliates; special provisions under water's edge election. N.H. Rev. Stat. Ann. § 77-A:4.
NJ	50% exclusion generally; 100% of dividends from 80% owned subsidiaries. N.J. Stat. Ann. § 54:10A-4(k)(5).
NY	100% deductible if from more than 50% owned subsidiary; 50% deductible otherwise. N.Y. Tax Laws § 208.9.
OH	Federal dividend deduction plus exclusion of all dividends where payor at least 25% owned by payee, and all dividends of foreign subsidiaries and affiliates. Ohio Rev. Code Ann. § 5733.04(I) and § 5733.042(A)(6).

STATE	DIVIDEND DEDUCTION OR EXCLUSION
RI	Federal dividend deduction plus exclusion for dividends on income taxed by R.I. R.I. Gen. Laws § 44-11-11 and § 44-11-12.
TX*	All dividends included in net taxable earned surplus, except dividends from certain foreign subsidiaries and affiliates. Tex. Code Ann. § 171.110.
VT	Federal dividend deduction. Vt. Stat. Ann. tit. 32 § 5811(18).
VA	Federal dividend deduction plus exclusion for dividends from 50% owned subsidiaries to the extent included federally. Va. Code Ann. § 58.1-402(C)(10).
WI	Exclusion for dividends from certain Wis.-taxed payors, and from 80% owned subsidiaries; "dividends received" excludes foreign taxes deducted federally. Wis. Stat. Ann. § 71.26(3)(j).

* Effective January 1, 1992, Texas enacted a tax on the "net taxable earned surplus" of corporations. Tex. Code Ann. § 171.002 *et seq.*

AMICI CURIAE CORPORATIONS	COMMERCIAL DOMICILE*
American General Corp.	Texas
American Home Products Corp.	New York City
Amway Corp.	Michigan
ASARCO Inc.	New York City
Asea Brown Boveri, Inc.	Connecticut
Ashland Oil Inc.	Kentucky
Avon Products, Inc.	New York City
Beatrice Co.	Illinois
Borden Inc.	New York City
Chevron Corp.	California
Coca-Cola Co.	Georgia
Colgate-Palmolive Corp.	New York City
Ford Motor Co.	Michigan
General Mills, Inc.	Minnesota
Georgia-Pacific Corp.	Georgia
Household International, Inc.	Illinois
ICI Americas Inc.	Delaware
International Business Machines Corp.	New York State
International Paper Co.	New York State
James River Corp. of Virginia	Virginia
Limited Stores Inc.	Ohio
Loews Corp.	New York City
Mead Corp.	Ohio
Mobil Oil Corp.	Virginia
NCR Corp.	Ohio
Phillips Petroleum Co.	Oklahoma
Premark International, Inc.	Illinois

AMICI CURIAE CORPORATIONS	COMMERCIAL DOMICILE*
RJR Nabisco Holdings Corp.	New York City
Safeway Inc.	California
Scott Paper Co.	Pennsylvania
Square D Co.	Illinois
W.R. Grace & Co.	New York City

* Sources: *Standard & Poor's Register of Corporations, Directors and Executives,* Vol. I (1992); *America's Corporate Families,* Vol. I (Dun's Marketing Services 1991).